



Ninety-Eighth Legislature - First Session - 2003
Introducer's Statement of Intent
LB 128

Chairperson: Mark Quandahl
Committee: Banking, Commerce and Insurance
Date of Hearing: January 28, 2003

The following constitutes the reasons for this bill and the purposes which are sought to be accomplished thereby:

LB 128 makes a number of amendments to articles 3 & 4 of the Uniform Commercial Code, as follows:

I. LOST INSTRUMENTS – UCC SECTION 3-309

LB 128 provides clarification regarding the treatment and enforceability of lost instruments under UCC Section 3-309.

The provisions of UCC Section 3-309 relate to the ability of a transferee of a lost instrument to enforce that instrument. Under current law, the transferee of a lost instrument must not only prove that its transferor was entitled to enforce the instrument, but that the transferee was in possession of the instrument at the time it was lost. With the changes proposed under section 3 of LB 128, the transferee of a lost instrument will only need to prove that its transferor was entitled to enforce the instrument, not that the transferee was in possession at the time the instrument was lost.

II. DEMAND DRAFTS

A demand draft is a type of check printed by a merchant or telemarketer that has purportedly obtained permission from a customer to create a draft drawn on the customer's account. The customer may authorize the merchant or telemarketer to create the draft by providing his or her name, address, and bank account number, which is then printed onto a demand draft. The draft is processed through normal channels via deposit of the draft into the merchants or telemarketers bank account with presentment by the merchants or telemarketer's bank (the "depository bank") for collection to the customer's bank (the "payor bank"). If a demand draft has been authorized by the customer, the draft is a "properly payable" item and must be honored by the customer's bank.

Under current UCC law, the customer's bank (the "payor" bank) is responsible for any item it honors, except when it can prove that another party acted negligently or with knowledge of a forgery. This rule rests on the notion that the payor bank is in a much better position than the depository bank to access the authenticity of the signature on an item, because the signer of the check is the payor bank's customer.

However, in the case of demand drafts, there is no signature to review, making it difficult for the payor bank to determine whether its customer authorized the draft which has been processed. Furthermore, with modern processing systems, very rarely does an employee of the payor bank physically view the draft for accuracy, validity or the customer's signature.

The provisions of LB 128 relating to demand drafts propose to shift the burden of loss in demand draft fraud cases from the payor bank to the depository bank. As a result, when a payor bank is required to make restitution to a customer's account resulting from an unauthorized demand draft, it may, under LB 128, recover its losses from the depository bank. This results from the requirement under LB 128 for a depository bank presenting a draft for payment to the payor bank to extend a warranty that the draft is authorized. In instances where the draft is not in fact authorized, the payor bank will have a breach of warranty claim against the depository bank.

LB 128 also contains "choice of law" or "reciprocity" provisions relating to demand drafts which ensures that transferees of demand drafts in states where the payor or payor bank is liable for payment on a fraudulent draft would not be able to pass that responsibility on to a transferor or depository bank in Nebraska.

Principal Introducer:

Senator Mark Quandahl